



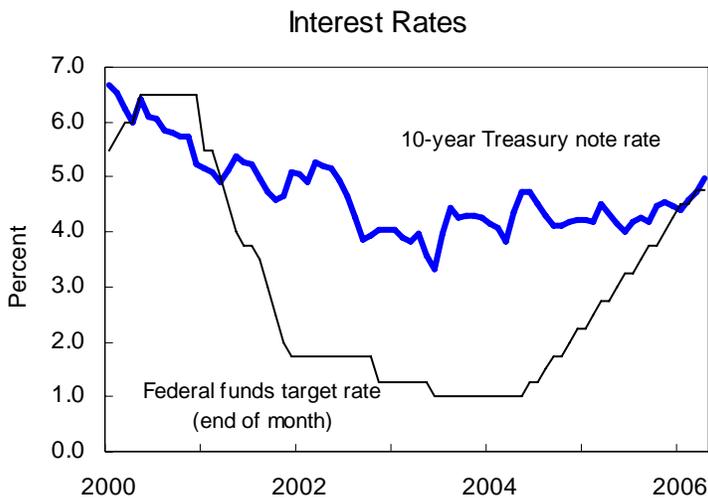
WEEKLY ECONOMIC DIGEST



JOINT ECONOMIC COMMITTEE – DEMOCRATIC STAFF
SENATOR JACK REED (D-RI) – RANKING DEMOCRAT

May 16, 2006

Fed Raises Rates Again, but Future Actions Will Depend on Data



Source: Board of Governors, Federal Reserve System.



Source: Census Bureau, U.S. Department of Commerce.

- **The Fed raised short-term interest rates again.** The Federal Reserve raised its target for the interest rate on federal funds by $\frac{1}{4}$ percentage point to 5 percent last week. That increase was the Fed's 16th consecutive $\frac{1}{4}$ -point hike in short-term rates since June 2004 when the target rate was 1 percent (see top chart). In contrast, long-term interest rates have risen by less than a percentage point since mid-2004.
- **The future direction of monetary policy is uncertain.** In announcing the rate change, the Fed noted that economic growth is likely to moderate following the first-quarter rebound and that labor costs and inflation expectations remain contained. But it cautioned that the run-up in energy prices has the potential to increase inflationary pressures, saying that the future direction of monetary policy will depend on "the evolution of the economic outlook as implied by incoming information."
- **Retail sales moderated in April.** Total sales at retail establishments and food services grew by 0.5 percent last month, after rising 0.6 percent in March. Sales at automotive dealerships were down 0.4 percent, but higher gasoline prices contributed to a 4.6 percent increase in sales at gas stations. Total sales were a solid 6.6 percent above their level twelve months earlier, with half of that gain coming in this year's strong first quarter.
- **The trade deficit narrowed unexpectedly in March.** The deficit for international trade in goods and services (imports minus exports) fell by \$3.6 billion in March from \$65.6 billion to \$62.0 billion. The drop in the deficit reflected a \$1.5 billion drop in imports—stemming from a drop in the value of oil imports—and a \$2.1 billion increase in exports. The narrowing in the trade gap came as a surprise to financial markets, which had expected the trade gap to widen to \$67 billion. Despite recent narrowing, the trade deficit remains large (see bottom chart).

The Economy at a Glance	Apr	Mar	Feb	Jan	2006 Qtr 1	2005 Qtr 4	2005 Qtr 3	2005 Qtr 2	2005	2004
Economic Activity										
Real GDP (% growth)	—	—	—	—	4.8	1.7	4.1	3.3	3.5	4.2
Industrial Production (% growth)*	n.a.	7.4	6.2	-4.7	4.5	5.3	1.4	1.6	3.3	4.1
Capacity Utilization (level, %)*	n.a.	81.3	81.0	80.7	81.0	80.5	79.8	79.9	80.0	78.6
Civilian Unemployment Rate (level, %)	4.7	4.7	4.8	4.7	4.7	5.0	5.0	5.1	5.1	5.5
Housing Starts (thousands)*	n.a.	1960	2126	2307	2131	2059	2101	2044	2072	1950
Real Disposable Personal Income (% growth)	n.a.	1.2	2.4	0	3.2	6.7	-1.4	0.2	1.4	3.4
Retail Sales (% growth)	6.0	7.8	-9.7	43.2	13.3	1.9	8.6	9.5	7.2	6.2
Personal Saving Rate (level, %)	n.a.	-0.8	-0.6	-0.6	-0.7	-0.2	-1.6	-0.2	-0.4	1.8
Inflation & Productivity										
CPI-U Inflation, all items (% growth)*	n.a.	4.9	1.2	8.7	2.2	3.2	5.5	3.7	3.4	2.7
Core CPI-U Inflation (% growth)*	n.a.	3.7	1.2	2.4	2.4	2.4	1.6	2.0	2.2	1.8
Employment Cost Index (% growth)	—	—	—	—	2.4	3.2	3.2	2.8	3.3	3.7
Output per Hour (% growth)	—	—	—	—	3.2	-0.3	4.2	2.4	2.7	3.4
Financial Markets										
T-bill Rate, 3-month (level, %)	4.60	4.51	4.43	4.24	4.39	3.83	3.36	2.86	3.15	1.37
T-note Rate, 10-years (level, %)	4.99	4.72	4.57	4.42	4.57	4.49	4.21	4.16	4.29	4.27
Federal Funds Rate (level, %)	4.79	4.59	4.49	4.29	4.46	3.98	3.46	2.94	3.22	1.35
Dow Jones Industrial Avg (index level)	11235	11144	10971	10872	10996	10616	10544	10382	10548	10317

Sources: Bureau of Economic Analysis, U.S. Department of Commerce; Bureau of the Census, U.S. Department of Commerce; Bureau of Labor Statistics, U.S. Department of Labor; Board of Governors of the Federal Reserve System; Wall Street Journal; and Haver Analytics.

Notes: Except where otherwise noted, values in the table represent percentage growth measured at seasonally adjusted **annual** rates. Growth in retail sales includes food services. Core CPI-U inflation is the percentage change in the CPI-U excluding food and energy as reported by the Bureau of Labor Statistics. The Employment Cost Index is for civilian workers. Productivity is output per hour for private nonagricultural establishments. The 3-month Treasury bill rate is the secondary market rate.

n.a. Denotes that data are not yet available.

* Subject to revision over the next week.

Upcoming Economic Releases:

- **New Residential Construction: April 2006** [Release: Tuesday, May 16]
- **Producer Price Indexes: April 2006** [Release: Tuesday, May 16]
- **Industrial Production and Capacity Utilization: April 2006** [Release: Tuesday, May 16]
- **Consumer Price Index: April 2006** [Release: Wednesday, May 17]